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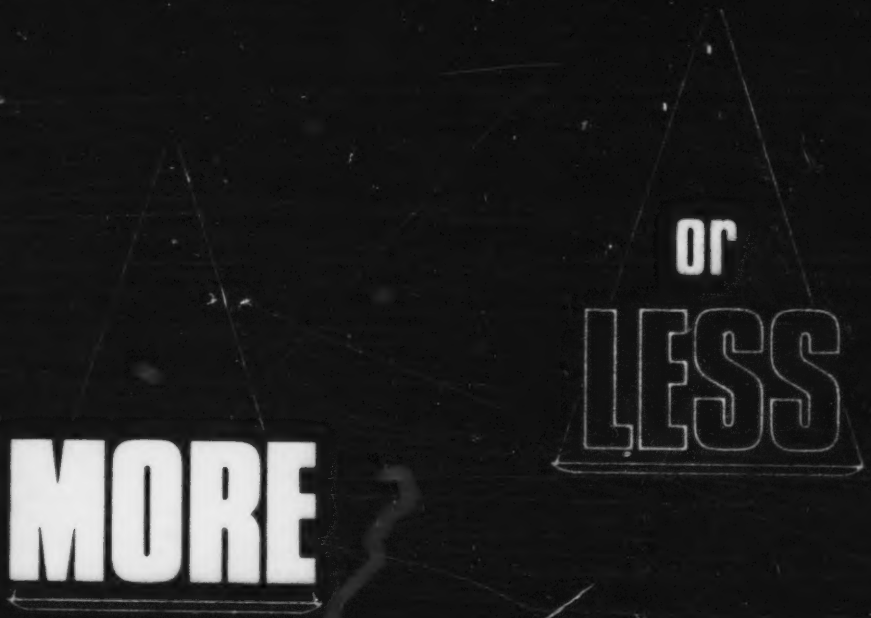

THAN YOU BARGAINED FOR

Message From the Minister

Planning for retirement requires careful consideration by each individual during his or her working years. If you are now participating in a union pension plan, you may be asked to become a trustee of the fund. In such a role, you will be sharing the responsibility with your fellow trustees in making sure that the future pension of many people involved in your pension plan is protected and will continue to meet the needs of those people at retirement.

This booklet outlines the responsibilities of the trustees, as well as many other aspects of the operation of a trusted pension plan, which is usually the type of plan implemented by union and labour groups.

All pension plan members will benefit from the information contained herein. I hope this booklet will be used frequently as a reference source and an education guide to promote awareness of a vital topic in each of our lives.

Mary Beth Dolin
Minister of Labour & Manpower

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Introduction

It has been our pleasure over the past years to consult with the Manitoba Federation of Labour on matters relating to pensions for union members. There has always been representation by the MFL on the Pension Commission itself and the Office of the Superintendent of Pensions has been involved in numerous meetings and extensive seminars for union delegates to promote a greater awareness of pension plans and their own special benefits as well as improvements which could be made to existing plans.

The Pension Commission has sponsored two such educational seminars to date. One in March of 1980 and one in February of 1981. Both recorded attendances in excess of 200 and were comprised of union delegates from Winnipeg as well as rural and northern areas. The two day seminars were structured to allow as much audience participation as was possible and this booklet is a direct result of the interest generated by the seminars.

In order to insure that the information concerning pension plans and specifically union pension plans reaches those members who could not attend the seminars, we have summarized the topics and provided you with a handy reference booklet.

At the conclusion of each topic, we have included some questions and answers which were raised during the workshop at the seminars.

As we stress during all pension seminars, the Office of the Superintendent of Pensions is available for you to call on for any general or specific pension queries.

We hope that with this booklet as an information source you will at least "get what you bargain for".

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OTHER PENSION COMMISSION PUBLICATIONS:

"SOME OF THE THINGS YOU WANTED TO KNOW ABOUT PENSIONS. . . BUT WERE AFRAID TO ASK"

"SISTER WILL YOU HAVE A DIME?"

SECTION 1 - The Role of the Trustee

Here are some technical terms you will come across when reading this Section. You should familiarize yourself with them before reading this part.

Beneficiary
A person for whose benefit the property is held and the trust is created.

Benefit
The amount payable to a participant or his beneficiaries under a plan.

Collective Agreement
The document containing the conditions of employment negotiated between the employer and the union and agreed to by the employees covered by it — this is usually the source calling for the creation of a trust.

Trust
The relationship which arises with respect to property and involves certain duties imposed upon the holder of the title to the property to deal with it for the benefit of another person or persons.

Trust Agreement
The document containing the conditions under which the trustees administer the trust.

Trust Fund
The legal entity which receives the property and disburses benefit payments to the beneficiaries.

Trustee
The person who holds legal title to the property and who accepts the specific duties pursuant to the trust.

Trusteed Plan
A plan under which contributions are paid to and invested by a trustee. The duties of the trustee as set forth in the trust agreement or indenture may range from mere investment and conservation of the funds, subject to various restrictions, to complete administration of the plan. Under a fully trusteed plan, benefits are payable from the trust fund directly, usually on the basis of determinations as to eligibility and pension amounts by a person or retirement committee appointed by the employer. Under some hybrid plans, the trustee may be authorized or required to provide benefits by buying an annuity from an insurance company for each employee at the time of retirement.

Jointly Trusteed Plan
A plan which is governed by a board of trustees consisting of equal nominees from both the employer and the union.

A) Duties

You have been approached with the idea of becoming a trustee of your pension fund. What, you ask yourself, does it mean to be a trustee?

Before we can answer that question it must be explained what a pension trust is. Primarily it is a fund into which monies are paid with the purpose of providing individuals with an annuity. The date at which the annuity begins is the occurrence of a specific event, normally when the individual retires.

The pension trust fund comprises property (investments) and it is the relationship to this property which imposes certain duties and responsibilities on the holders (the trustees) of title to the property to deal with it for the benefit of other persons.

There must be at least three trustees appointed to administer any given pension trust, usually there are more. Often there is a board of trustees made up of equal representation from the employees and the employer(s). The board of trustees, once established, has power and authority from two sources. The first is The Provincial Trustee Act and the second is the trust agreement itself.

The Trustee Act sets out rights, duties, and obligations of the trustees. However, this Act states specifically that the trustees are subject to the terms of their trust agreement; thus the trustees' primary responsibility is to the trust agreement.

The trust agreement is particularly important in that it must grant the trustees sufficient discretionary powers to fulfill the objectives of the pension plan, yet it must limit their activities within the dictates of the provincial legislation.

Trust agreements can be very lengthy (as many as 50 pages) and go into great detail. They often can be worded in "legalese" and because of this, you would have to be a "Philadelphia lawyer" to understand it. It is important to remember that, as a trustee, you will be bound by the trust agreement. You should know what it says and it is your right to have it explained.

Some of the major duties and responsibilities of a pension fund trustee are as follows:

1) **to receive contributions** — the basic purpose of a trust is to receive contributions, invest and reinvest them, and, ultimately to pay out benefits. While anyone can administer a pension fund (the Union office, a permanent employee, etc.) it is the normal practice for the trustees to employ a professional fund administrator. The cost of this is usually borne by the trust fund, but can be paid entirely by the employer.

2) **to invest funds** — if the fund is small the administrator may also be the investment manager. However, professional investment advice is often necessary. Many companies perform the dual function of administrator and investment manager. It must be borne in mind that the primary responsibility is to the beneficiaries of the trust (the pension plan participants) and their interests come before all others. Because of this responsibility the safety of the investment is as important as the rate of return gained on the investments, if not more so!

3) **to determine eligibility rules** — this may sound like an unimportant item, however, inasmuch as the purpose of the trust fund is to provide benefits to individuals, determining eligibility for those benefits is crucial. Professional assistance is usually employed in this area.

4) **maintenance of proper accounts and records** — remember you are dealing with funds belonging to other people and it is vital that proper accounting be maintained, both from their stand point and yours. This function is usually performed by the administrators and the trust fund's auditor.

5) **be knowledgeable of current trust fund activities** — some trustees take their positions lightly and are not aware of all the activities of the fund. It is important that you be aware of the functioning of the trust fund and plan so that, if a problem arises, all of the trustees will be equally capable of making a decision.

6) **to maintain proper minutes of all meetings** — it is important to have an accurate set of minutes for all meetings. In this way any decisions made by the trustees can be substantiated should any questions or investigations arise. As well the auditor of the fund, in the course of his duties, will require the minutes for review.

7) **to act in the best interests of and protect the beneficiaries (members)** — as a trustee you are bound to act solely on the basis of what is best for the beneficiaries. There is no such thing as a "management trustee" or a "union trustee", there are simply trustees. It may be difficult to "change hats" as it were, particularly at negotiation time, but it is imperative that the trustees be able to do so.

These are some of the major functions of pension fund trustees. The precise definition of all the duties and responsibilities are laid-out in the trust agreement itself and can take several pages. Remember you are legally bound by the trust agreement and it is up to you to be aware of what it says.

B) Liabilities

The first question many people would ask themselves when considering taking on the position of a pension fund trustee is: "As a trustee would I be liable for any short-fall of monies in the pension fund?" The answer is YES, but read on; its not as bad as it sounds.

The law requires that a trustee carry out his duties using "no higher diligence in the execution of his office than a man of ordinary prudence would exercise in the management of his own affairs." What this means is that for a trustee to become liable he would have to be extremely negligent in his duties. Furthermore, due to the level of expertise available to trustees and to the high degree of dedication trustees exhibit, it would be almost impossible for them to establish pension fund deficiencies, other than out and out theft of monies.

Deficiencies can happen, however, and the following specific examples will highlight the fact that the trustees would have to be very negligent to allow them to occur:

1. **Misappropriation of funds** — this would be very similar to outright theft and trustees would have to answer for any misappropriations.
2. **Mismanagement by incompetence or negligence** — this would involve failure by the trustees to accept professional advice including legal, actuarial, or investment counsel. It would also involve failure to maintain proper books and records.
3. **Approval of excessive costs** — trustees have been known to approve excessive fees for salaries, expenses, etc. all paid out of trust funds.

4. **Conflict of Interest** — mostly involves improper investment of funds whereby such investments benefit the trustees themselves.

You may think these are extreme examples but events such as the ones described above have actually occurred. You can easily see that for a trustee to "unknowingly" become responsible for a pension fund deficiency would be next to impossible.

You Asked Us . . .

Does the Trustee Serve the Employer or the Employee?

Neither. The Trustee's prime responsibility is to the fund itself. As was mentioned previously, a Board of Trustees is usually representative of the employer and the employees. A member or members may be elected by the employee body to represent them. This member(s) would be able to relay any special employee concerns to the Board on their behalf. As a Trustee, however, the prime concern is the best interest of the fund and the employees in order that promised pension benefits may be protected now and in the years to come.

Is it Possible to Obtain a List of Trustees for One's Own Plan?

Certainly. The plan administrator could provide you with a listing of the Trustees as could the Pension Commission of Manitoba upon request.

What Procedure is Involved to Change the Structure of the Trustees?

There must be at least three trustees appointed or named in the agreement to attend to the pension trust fund. This is a legal requirement. As mentioned previously, however, there are usually more than three trustees, and very often a Board of Trustees who conduct regular meetings to attend to the trust fund business. Additional Trustees may be appointed from time to time or the number of trustees may be reduced (no less than three).

Is the Trustees Act Available to Anyone?

The Trustees Act, being a provincial statute, is available to anyone who wishes a copy. Copies may be obtained at the office of Queen's Printer located in the Manitoba Archives Building, 200 Vaughan Street, Winnipeg, Manitoba R3C 1T5.

Does a Member Have the Right to Appeal a Decision Made by the Trustees?

Yes, an appeal can be launched through the Trustees or by contacting the Pension Commission of Manitoba.

SECTION 2 - How To Set Up A Pension Plan

Here are some technical terms you will come across when reading this Section. You should familiarize yourself with them before reading this part.

Contributory Plan
A plan into which both employees and employers make payments for the purchase of pensions.

Non-Contributory Plan
One in which all contributions take the form of payments made by the employer.

Defined Benefit Plan
A pension plan which provides an Annuity whose amount is determined by a Defined Benefit Formula.

Money Purchase Plan
A pension plan in which contributions of employee and employer (commonly 4 per cent and 4 per cent) are accumulated, at interest, to purchase at retirement whatever annuity the resulting sum will buy. The employer's contributions may be subject to vesting conditions similar to those in other types of plans.

Annuity
A specified sum paid each year for a given number of years or for life. Often used synonymously with "pension" to mean a specified payment per month or year for the balance of the life of a retired employee.

Defined Benefit Formula
A generic term for any benefit formula which specifies, for a given level of income and period of service, the exact amount of deferred annuity that may be expected. Unit benefit, flat benefit, and final average formulas are all of the defined benefit type to be distinguished from Money Purchase Plans.

There are many steps which must be followed in the establishment of a new pension plan. These include, in chronological order, the following:

1. Establish a committee to study and oversee all of the remaining steps with respect to the establishment of the pension plan.
2. Engage the services of an expert in the employee benefits field, such as a plan administrator, an actuary, and/or a pension consultant.
3. Meetings should then be held between the pension committee and consultant to determine what the aims and objectives are and which type of plan may be best suited to fulfill those needs.
4. In conjunction with the consultant, decide upon the final terms of the pension plan, the ground rules to be set out for the investment management and the administration of the pension fund.
5. The consultant should then provide the committee with cost estimates for the various types of plans that would be appropriate for the objectives laid out earlier.
6. The pension committee, having decided on the type of plan required and the costs involved, should decide whether the funding is to be on a employee/employer basis or solely on an employer basis, i.e. whether it is to be a contributory or non-contributory pension plan.
7. The pension committee should obtain the approval of all participating employers and local unions.
8. The pension plan must be registered with all the appropriate authorities, and once this step has been completed, presentation to, and enrollment of employees can be accomplished.

There are major steps to be followed in the establishment of a pension plan. The most crucial area is the formation of a competent pension committee which will not hesitate to call in the assistance of experts in the pension field where needed.

Whether or not a union is involved in the organization of a pension plan, the employer has usually assumed responsibility for its administration and for the security and investment of a fund. This is due to the fact that the employer is normally the one who makes the ultimate decision to establish the pension plan as well as being the main source of funds and financial commitment towards the operation of the pension fund. There are, however, two types of arrangements under which employers and employees jointly participate in the running of pension plans, namely a joint trustee-ship and a joint supervision arrangement.

Under the joint trustee arrangement, representatives of both employees and employers share responsibility for the security and investment of the funds held on behalf of the participants in the pension fund. Under this kind of arrangement the trustees (both employee and employer) have joint control over the entire operation of the plan. On the other side of the coin, joint supervision of a pension plan usually means a committee is established representing management and employees and this committee oversees the administration of the plan but assumes no direct responsibility for the financial security or policy matters. In this type of situation it is the employer who retains control over the management of the pension fund.

This is not to say that there are no safeguards in this type of plan.

In recent years a number of protective measures have been taken on both a federal and a provincial level to guarantee that pension funds are pro-

perly administered and safeguarded. These include requirements of the Department of National Revenue through The Income Tax Act of Canada and provincial legislation such as The Pension Benefits Act of Manitoba and other provincial legislation.

Another issue of concern is the ownership of pension funds. Many pension plan members consider their pensions as deferred wages to be paid from funds set aside out of current earnings during their working lives. They feel, perhaps justifiably, that contributions paid into the plan are their property and should be controlled by them.

It is quite natural that pension plan participants would have a strong proprietary interest in their pension fund. To many of these members, the fund would appear to be the exclusive property of the employer and completely under his control. As mentioned elsewhere the rules governing a pension plan provide that a pension plan must be held in trust on behalf of the members of a plan. Pension plan sponsors may appoint trustees (some of whom may be employees) but there is a clear distinction in law and in fact between responsibilities of a company officer who is a trustee, meaning that an officer of the company must be able to separate responsibilities between company business and trust fund business. As a trustee his sole responsibility is to the trust fund and its beneficiaries. In addition at least one of the trustees can be neither an employer or an employee participating in that pension fund.

Some pension funds are held by insurance companies and not by a group of individual trustees. In this circumstance the pension plan is funded through a contract for insurance and premiums are paid to the insurance company as a third party in much the same manner as contributions are turned over to trustees under the previous arrangement. Therefore there is really no difference in principle between claims to ownership of funds held by an insurance company and those held by a corporate or individual trustee.

Pension plan members are understandably concerned with the security of the money that will provide them with their income after retirement. Therefore, any measures necessary (such as engaging the services of professionals) to improve the security should be taken advantage of rather than left to the responsibility of the individual pension plan members. Although employer and employees are both justified in taking close interest in their pension fund, for the safety of all concerned neither party is allowed to have complete control of the pension fund.

You Asked Us . . .

What Should the Minimum Contribution Rate be in Any Plan?

Many union negotiated pension plans are what is known as flat benefit plans. (This is fully explained in our other booklet, "Some of the Things You Wanted to Know About Pensions But Were Afraid to Ask?".) In this type of plan a level of pension benefits is decided upon (usually through the negotiation process). This is usually stated as an amount of pension per year of service worked, for example each member will receive $15.00 per month of pension per year of service worked. Once the benefit level is decided upon the actuary will then determine the contribution level needed to support the agreed upon pensions. The contribution rate is often expressed as so many cents per hour worked.

If the type of plan is other than a flat benefit, for example a money purchase plan, it is the contribution level that is usually decided upon first. Under a money purchase plan, the Department of National Revenue has a regulation stating that the contributions can be no less than 1% of salary in any given year. The general level of contributions one most often sees in a money purchase pension plan is in the neighbourhood of 4 - 6%, often integrated with contributions to the Canada Pension Plan.

Who Determines the Amount of Pension Received From a Money Purchase Pension Plan?

Under a money purchase pension plan the pension is provided through an annuity policy. At the present time only insurance companies are allowed to market annuities and therefore the pension must be purchased from one of these firms. Each insurance company will have a table of annuity rates which will state how much pension you can receive for a given sum of money. It is important to note that there are no standardized annuity rates. Each insurance company will have its own rate which could be better or worse than the next company. It is very important to be aware of this difference, and to ensure that all members receive the best pension possible it is advisable that the annuity market be canvassed to determine which insurance company will provide the most pension at a given point of time. A rough rule of thumb for determining the amount of pension provided for a given sum of money is that for every $1,000.00 available you will receive $10.00 per month of pension. In times of high interest rates this can change quite substantially so that you will only need $700.00 - $800.00 to purchase $10.00 a month of pension. On the other side of the coin in times of low interest rates you may require $1100.00-$1,200.00 to purchase $10.00 a month of pension.

SECTION 3 - The Role Of The Administrator

Here are some technical terms you will come across when reading this Section. You should familiarize yourself with them before reading this part.

Benefit
The amount payable to a participant or his beneficiaries under a plan.

Widows & Orphan's Benefit
On the death of the employee either prior to or following retirement, the widow is entitled to a life income generally equal to a percentage of the deceased's accrued pension credits at the date of death, or actual pension if death follows retirement. Pension can be made payable to orphans until they have attained a certain age.

Death Benefit
The sum of money paid in the event that a member of a pension plan dies before his pension has commenced (i.e., in the period of deferment).

Any person, union, employer, or company with specialized knowledge and training can be employed to administer the operation of your pension plan. Depending on the size of the plan and the number of members, this task is usually left to professionals, however, the union does play a definite role in plan administration. Some of the major areas of involvement for the union would be as follows:

1. Communicating the wishes and objectives of the membership;
2. Providing the necessary data and other pertinent information necessary for the operation of the plan;
3. Providing continuous up to date information as to the methods of funding, the amount of funding, etc.;
4. Providing ongoing backup and promotion in order to assure the success of the plan and that it fulfills its objectives;
5. Assisting in development of reciprocal agreements with other plans and/or locals in order to ensure the highest degree of portability of pension benefits,
6. Providing full committee representation at all meetings and to make sure that the committee has all necessary plan documentation and is fully knowledgable of the plan operation. Remember the committee (trustees) are responsible for the direction and the financing for the welfare of other persons.
7. Taking an active role in the direction of the professionals employed with respect to the pension plan such as lawyers, actuaries, investment managers and auditors, etc.,
8. Participating in educational seminars to keep abreast of current pension thinking in issues and legislation.

These are only a few areas in which the union can become involved. No doubt there are many many more, and your own particular experience will dictate other areas in which you may wish to become involved.

Now that we know who can administer a plan and what the union's involvement might be, we can now look at exactly how a plan is administered. The job of the administrator, no matter who that may be, in very simple terms, is to keep track of what comes into the fund (contributions) and what goes out of the fund (payment of claims and benefits). In more technical terms the administrators job can be broken down into three areas, mainly,

1. Maintenance of fund records,
2. Processing the claims of the pension fund, and,
3. Reporting to and for the trustees.

In the course of these duties the administrator, if he is doing his job properly, should be in constant communication with all of the parties involved, i.e. the employer, the union, the trustees, the consultant, the actuaries, the lawyers, the investment manager, and perhaps the most important of all, the members of the plan who ultimately receive benefits.

We will now consider each of these areas in more detail.

Record Maintenance

Of all the functions of the administrator this is probably the most important. All of the other duties including assisting individuals in the choice of benefit payouts, reporting to the trustees, calculation of benefits, and determining

eligibility for benefits, depends upon prompt and easy access to accurate information.

You may think that keeping up to date records of a pension fund is a relatively straight-forward task. This is not the case. Included in the record keeping function are all the related duties such as:

1. All banking activities related to fund monies including the reconciliation of accounts.
2. Keeping track of employee eligibility information.
3. Maintaining all fund records such as the rules and regulations of the pension plan itself, plan descriptions and all the associated policies, and,
4. Maintaining a system of checks and balances to protect the trust fund from unauthorized or illegal transactions.

The Disposition of Benefits (Handling of Claims)

This is also an extremely important function of the administrator as he is often the individual who deals directly with the plan participant. In order to do this job efficiently, the administrator usually employs competent, friendly, and tactful individuals who are best qualified to assist the plan participants in the settlement of claims.

Some of the functions included in the handling of the claims are:

1. Offering assistance and counseling to plan participants,
2. Handling all direct communications with the plan participants,
3. Assist in the completion and the provision of necessary forms,
4. Providing annual statements to the plan participants, accurately reflecting their current status in the plan, and,
5. Providing for the compiliation and distribution of monthly pension cheques or arranging for this service to be performed elsewhere. (e.g. the purchase of an annuity).

It is important to remember that for the plan participants, the administrator is often their sole contact with their pension plan and thus the person fulfilling this role must be well versed in the plan provisions and be able to communicate well with the participants.

Reporting

The third major function of the administrator is reporting to the trustees and on behalf of the trust. Some of the duties which fall under this responsibility are as follows:

1. Furnishing periodic financial statements to the trustees and provide an annual report on the performance of the trust fund.
2. Preparing the forms and reports required by the various federal and provincial agencies such as the Department of National Revenue and the Pension Commission of Manitoba.
3. Co-ordinating and attending trustee meetings, and reporting to the trustees on the operations of the fund. (This is why you often see a representative of the administrator being appointed to the board of trustees.)
4. Preparing the cheques and disbursement statements for the trustees.

5. As mentioned earlier, providing members with annual reports as to their current status in the plan.
6. Providing back up material to other professional bodies retained by the fund such as the consultant, the actuary, and the auditor.

The foregoing points serve to highlight the broad basis upon which the administrator must perform his duties. The administrator should, and can, cover all the possible aspects of the operation of the pension fund.

It is a role with many diverse functions requiring detailed knowledge which deals with a corresponding variety of people. As a result, the administrator must become totally knowledgable about a pension fund and this familiarity, combined with a high degree of professionalism, makes the administrator an integral part of the successful operation of any pension fund.

You Asked Us . . .

Does the Administrator Supply Employees with Financial Statements?

Yes. Each year each employee receives a statement indicating the status of the pension plan. The statement can be in various formats and some are much more detailed than others. However, the Pension Benefits Act of Manitoba states that at least basic information must be provided to the plan participants. The statement must show the total contributions made to the fund and must include the balance in the fund at the previous fiscal year. All expenditures from the fund must be shown; pension payments, cash withdrawals on death and terminations of employment as well as any administrative costs during the year must be listed separately. The statement should conclude with the balance of the fund at the end of the year under review. Many times this information is posted on a central bulletin board for all employees to review at will.

Sometimes, each employee is provided with an individual statement showing the amount he or she has accumulated in the past year and the total amount of pension accumulated to date. Individual statements are more costly to prepare than a general statement, and consequently the Board of Trustees usually opt for a general statement.

Is There a Time Limit on the Receipt of Financial Information?

Yes. A statement such as the one previously mentioned must be posted on the bulletin board or sent to the plan participants within nine months from the conclusion of the plan's fiscal year.

Who Pays for Expenses Related to the Operation of the Pension Plan?

Depending on the circumstances and what kind of agreement has been made, the expense charges for the plan's operation are usually paid directly through the fund itself. Requests for payment of expenditures are reviewed by the Board of Trustees and a cheque would be issued by the Administrator. The specifics of the expenditures should be itemized on the financial statement of the plan, as mentioned previously, and would include such costs as any actuarial work done, provincial/federal filing fees and the cost of the day to day operation of the plan itself by the administrator. In some instances, the employer may pay the total cost of expenditures and sometimes the cost is shared by the employer and the employees.

SECTION 4 - The Role Of The Actuary

Here are some technical terms you will come across when reading this Section. You should familiarize yourself with them before reading this part.

Age Distribution
A classification of individuals according to their ages, such as the numbers of males aged 20-24, 25-29, etc.

Actuarial Equivalent
The amount of annuity or pension that can be provided at the same cost as a specified annuity of a different type or a specified annuity payable from a different age. For example, according to the group annuity actuarial assumptions of one insurance company for male lives, a five-year certain annuity of $97 a month from age sixty-five is the actuarial equivalent of a life annuity of $100 a month; an immediate life annuity of $49.43 a month from age fifty-five is the actuarial equivalent of a deferred annuity of $100 a month from age sixty-five.

Benefit Formula
A rule by which the amount of a pension is calculated, the amount being determined by multiplying either some fraction of the earnings with respect to which contributions have been made, or a fixed dollar amount, by the years of pensionable service.

Current Service
Participation in a plan after its adoption. Hence current service benefit or credit is the amount of pension payable for each year of such participation, and current service cost is the estimated cost of providing pensions based on such participation; related terms are current service liability and current service funding.

Entry Age Normal Funding
The scale of level premium contribution rates that could prevail if all employees entered a pension plan at a specified age. Entry age normal calculations imply a staff to which no recruits are added above the specified age, except as casual labour or on the understanding that they cannot join the pension plan.

Funded
Having sufficient funds accumulated to meet all accrued liabilities. A pension plan is fully funded if annuities have been bought or sufficient money is available to provide all pensions earned to date. Plans are often described as funded if current service liabilities are funded and arrangements have been made gradually to fund the past service liability. An unfunded plan is a pay-as-you-go plan under which, without prior accumulation of funds pensions are paid when due as a current cost.

Funding Method
The method of accumulating funds for the payment of pensions, such as the single-premium, level premium or the level percentage of payroll method.

Life Expectancy
The average number of years the individuals of a large group of any given age and sex may be expected to live according to a specified morality table.

Level Premium Funding
A method of reckoning pension contributions at a uniform percentage rate over an employee's whole period of pensionable service to retirement or termination. It serves to anticipate, in the case of young employees, the higher contributions usually required as they grow older, and results in a larger average accumulation and hence larger earnings of interest.

Mortality Rate
The proportion of persons of given sex and age that dies in a year. For example, a table of rates would show that of 10,000 males reaching their 25th year of age, 13 may be expected to die before reaching their next birthday. Not to be confused with the ordinary or crude death rate which ignores differences in age and sex.

Past Service
Service rendered prior to the adoption of a pension plan for which pension credit will be given. Hence past service benefit or credit, past service cost, past service liability and past service funding.

Salary Scale
The levels of earnings, usually on a full-time basis, that are assumed for employees at successive years of age throughout a working life with a given employer. Necessary for estimating the future accrual of pension benefits and costs.

Separation Rate
The proportion of employees that cease to be on a pay roll in a given period. Includes temporary lay-offs of permanent staff and also lay-offs of casual labour; the separation rate exceeds the rate of permanent withdrawal and exaggerates the mobility of labour. The relevant rates for pension purposes are rates of job changing and termination.

Single Premium Funding
Under single premium funding, the employer's cost in any year in respect of any one individual is the present value at the latter's age of his pension and refund benefits for service in the year less the employee's contributions (if any). The employer's contribution required, for a year of service under a defined benefit plan, to provide a specified benefit at normal retirement age.

Terminal Funding
Instead of building up a systematic fund during the employee's period of service, the employer undertakes to purchase, from an insurer, an annuity of defined amount at the time of each worker's retirement from his service. There is no provision for those who leave prior to retirement. No assets are sequestered for the provision of accrued pension claims in the event that the employer ceases operation.

Termination Rate
The proportion of employed persons of given age that terminates during that year of age, for reasons other than death or retirement. The rates may be calculated with respect to (1) all those on a payroll, or (2) all those other than labour defined as casual or (3) members of a pension plan only. In non-contributory plans, where most of the staff automatically become plan members, there may be no difference between (2) and (3).

"What is an actuary?" "What does he do?" "Why do we need him?"

These are all questions which corne to mind when someone mentions the word actuary. The following discussion will answer all of these questions plus many other questions you may have concerning the role of the actuary.

In determining what an actuary is it is important to know the background and training a person must go through leading up to the designation F.C.I.A. — a Fellow of the Canadian Institute of Actuaries. First of all the person should have a basic mathematical aptitude which is generally followed by a university degree either in mathematics or administrative studies. There are also a few schools which specialize in actuarial mathematics. One of these is the University of Manitoba.

In order to qualify as an Actuary it is necessary to complete a series of 10 professional examinations which may take from 18 months, to 4 or 5 years on the average, to as long as 17 years. These courses and examinations are usually attempted while working for a life insurance or actuarial consulting firm.

When the examination procedure has been completed, the individual is given the designation a Fellow of the Canadian Institute of Actuaries, and is free to practice his trade in Canada. This is a highly privileged position since according to pension and insurance legislation of the federal and provincial governments, only a Fellow of the Canadian Institute of Actuaries is permitted to sign certificates which concern the solvency of pension plans and insurance companies.

When answering the questions "what does an actuary do?" and, "why do we need him?", it is better to take somewhat of a backhanded approach. First of all we can identify the problems being faced and then examine what role the actuary plays in the solution of these problems.

A pension plan represents a promise to pay a pension to an employee at some point in the future. An employee who joins a pension plan at age 25 and retires at age 65 may in fact still be collecting a pension at age 85 — some 60 years after he first became a member of the pension plan. This is almost certainly the longest of any financial arrangement an employee may be involved in, especially when you look at mortgages which are seldom longer than 30 years and also that companies will rarely borrow money over more than a 25 year term. The question being faced is how then should the companies arrange their financial affairs so that there will be sufficient money in the fund to pay the pensions promised some 60 years down the road? They could, of course, not make any plans at the present time, and just hope that they will still be in business when the pensions become due in the future.

This is obviously not a very satisfactory approach. First of all there is little or no security for the employee if the employer goes out of business. Secondly, if the employer does not fund the plan on an orderly basis, he will find that at some stage in the future he is going to have a severe cash flow problem when he is paying both wages and pensions. Lastly, in most provinces in Canada, including Manitoba, this approach is illegal under The Pension Benefits Act.

Faced with this problem of how to set aside funds in order to fulfill future promises regarding pension payments, the employer will call in his actuary. The actuary, by means of a number of assumptions, or educated guesses.

will be able to recommend to the employer how much he should put into the plan right now in order to pay for the benefits in the future.

One of the most important and vital assumptions the actuary will make is that of an investment return i.e. how much interest does he think the pension fund can earn over a given period of time.

For example, an investment return of 10% per year will mean that $1,000 invested now will be worth $1,100 in one years' time and $1,210 in two years' time. Therefore, if the actuary calculates that a pension benefit will cost $1,210 in two years time and he knows that the fund can earn 10% on the money, he will recommend that the employer put $1,000 into the fund right now.

It becomes important at this point to differentiate between an assumption and a prediction. In the previous example it has not been predicted that the fund will earn 10%, rather it has been estimated what will have to be put into the fund right now if in fact it does earn 10%. By way of another example let us look at what happens if the fund only earns 9% over those two years. The initial $1,000 payment will be worth $1,188 in two years time, so that in order to pay the $1,210 benefit an additional $22 will have to be put into the fund. On the other hand, if the fund earns 11%, it will be worth $1,232 at the end of two years, and there will be a $22 surplus in the fund. The employer can then use this either to cut his cost or to increase the benefit.

Coming up with a surplus in a pension plan rather than a deficit is better for all concerned and this is why the actuary will tend to use an interest rate that is somewhat lower than that which is currently obtainable in the investment market. To sum up, an actuary does not predict what the interest rate will be over the rest of the life of the plan, rather he assumes a rate of interest which the fund should be able to exceed. Of course he can be too conservative which will mean that his cost estimates are so high that the employer will not be willing to pay them.

In recent times, with interest rates at record highs, the job of the actuary is more difficult than ever. However, you have to remember that the major reason why interest rates are so high is because inflation is so high. Thus, even if you can invest your money at 15%, the real value of that money after a year has increased by 15% less the rate of inflation. The actuary, by being conservative in his assumptions, can allow the employer to offset the effects of inflation on the pensions without additional costs.

The second most important assumption that the actuary will make is the rate at which people will die — otherwise known as mortality. Once again an example will help to clarify the effect of mortality on the cost of pensions. Let us suppose that the life expectancy of an individual increased from 80 to 81 — this is quite small — about 1-1/4%. A pension for the same person would be payable for 16 rather than 15 years — an increase of 6-2/3%. Life expectancies have been steadily increasing over the last 50 years and while we can expect some slowing in this increase, it is fair to anticipate that this trend will continue for the foreseeable future.

There are other factors which must be taken into account. For example in a plan which bases pensions on earnings close to retirement, the rate of salary increase is vitally important. There are two basic types of salary increases — one, which is fairly general across the board, is linked with inflation and productivity. The other represents promotional and merit increase. In the actuary's calculations he would put the two together so that the

younger employees would be assumed to get larger increases than older employees.

Another major factor in the calculation process is the rate of termination of employment. When an employee terminates his employment, there is generally a profit to the pension plan. If no account were taken of these terminations in advance, a larger surplus would occur at the next examination of the pension fund and this is a technique which is often used as a conservation approach.

There are a host of other factors which may be taken into account. Where a plan is integrated, future increases in Canada Pension Plan need to be taken into account. Where early retirement is allowed, some assumption is needed about how many people will choose such early retirement. Additional factors will include a disability provision and whether or not you have a spouse at retirement and how old he or she is.

All of these assumptions represent the nuts and bolts on which the actuary will base his valuation on the pension fund. We will now look at the valuation process.

The Pension Benefits Act requires that a valuation be performed upon the establishment of a plan and at least every three years thereafter. Many employers have started to realize that, for larger funds at least, things can happen so quickly that it is often advisable to have the valuation every two years or even every year.

What is the purpose of a valuation? First of all it is a progress report in which the actuary looks at the assets of the fund and compares them with the liabilities of the fund. He calculates the liabilities by using the assumptions which were outlined earlier. From a second point of view the actuary wants to find out if the current assets, together with future investment returns at the rate assumed in the valuation, will be sufficient to pay all the future pensions and other benefits which have been earned up to the date of the valuation. If there are sufficient funds, the plan is said to be in a surplus position and the employer can choose to increase benefits or reduce his future costs. On the other side of the coin if the funds are insufficient the plan is said to be in a deficit situation. The employer is then required by The Pension Benefits Act to pay additional monies into the plan to make up this deficit over a period of 5 years.

The other purpose of the valuation is to recommend to the employer future funding rates which will be sufficient to provide the benefits which have been promised in respect of future service. These two processes — the progress report and the future cost — will, hopefully, allow the employer to fund his pension plan without any nasty shocks while ensuring it will provide security of benefits to the employee.

Up to now we have discussed the actuary's primary function — the valuation of the pension fund which is primarily of interest to the employer in that it is this valuation that establishes his costs. You as a union member can certainly make use of the service of an actuary. Let us say that your contract expires in a very short time and one of the points you will be bargaining for is a 10% improvement in pensions. I'm sure that you will agree that it would be of great assistance in the bargaining process if you can go to the table asking for a 10% increase in pension and, having used the services of an actuary, having a report outlining the precise costs of such an increase.

You Asked Us . . .

If the Contributions are Increased in the Pension Plan Will the Benefits Increase as Well?

This is almost a question of putting the cart before the horse. Contributions to a pension plan are generally increased for one of two reasons. Those being;

1. An increase in the pension benefits has been negotiated and the contributions must be increased accordingly in order to fund the new benefit level properly.
2. The investments of the fund have not performed as well as expected, and the Actuary, in his review of the pension plan, reveals that there are insufficient funds to pay for the promised benefits. This is known as an experience deficiency and contributions must be increased to make up for this lack of funds.

Are There Any Laws Stating that an Actuary has to Review the Pension Plan?

Yes, The Pension Benefits Act of Manitoba contains stipulations that a pension plan must be reviewed at least every three years by an actuary. The actuary must prepare a report showing the current status of the plan i.e. whether or not there are surpluses or deficiencies, and what the contributions should be in the next three years to support the promised pensions. Please note that these regulations do not apply to a money purchase plan, which, because of the type of plan it is, is always full funded.

Who Decides on Which Actuary to Hire?

In general, the person (Union, employers, members) paying the administrative cost of the pension plan, which includes the actuary's cost, will decide on which actuary to hire. There are several actuarial firms which specialize in union negotiated pension plans and one of these firms is often selected.

Who Reviews the Actuarial Report?

The actuarial report is submitted to the Pension Commission upon completion. If the Commission is not satisfied with the results of the report or the assumptions used ,the report will be returned and will have to be resubmitted with revisions.

SECTION 5 - The Role Of The Money Manager

One of the most important and vital decisions trustees of the plan will ever make is where and how to invest the contributions flowing into the trust fund.

Because of the specialized nature of the investment process, the trustees almost invariably engage the services of a professional — an investment manager. Before going into what the investment manager does, it is necessary to explain a little bit about what kinds of investments are available for pension funds.

There are basically four types of investments in which pension funds typically place their funds. These are:

1. **Equity Investments** — these are investments in common stocks issued by companies and are bought and sold through the various stock exchanges throughout the world.
2. **Debt Investments** — these are investments in mortgages and bonds. The word debt comes the fact that mortgages and bonds represent a loan of monies with a promise of repayment at some point in the future. For example you may purchase a Canada Savings Bond which is in effect a loan of funds to the Government of Canada in return for which you receive a certificate stating that the amount of the loan will be repaid at some point in the future together with some interest earned.
3. **Guaranteed Investments** — these are investment vehicles that are guaranteed as to principal and interest — very much like a term deposit at a bank or a guaranteed investment certificate at a Trust Company.
4. **Commercial Paper** — also known as "short term paper". These are short term "30 to 90 day" investments in the money market, for example treasury bills issued by the Bank of Canada. This investment vehicle is not usually used as primary investment source; rather, it is an interim measure designed to ensure that there is no idle cash being held.

Before going into more detail it should be explained that any investment has two components — capital (actual dollars invested) and income (the dividends and the interest, etc.). While it can be said that all investments will yield some income, not all investments will guarantee the integrity of the capital component.

When investing in equities, for example, you may pay $1,000 for a given stock. This stock may be guaranteed to pay a dividend of 10%. At the same time the value of the stock could decline by say 7% (capital depreciation) and the net return would be 3% resulting in a year end value of $1,030. The value of the same stock could just as easily have gone up by 7% to 1,070 and this combined with the 10% payment of dividends would have yielded $1,170 or a 17% return.

This wide fluctuation in capital values can be called the risk factor. With equity investments the chance of spectacular gains exists but at the same time the chance of substantial loss also exists. This risk factor is one of the elements that must be considered by the investment manager when deciding which stocks to buy. There are many low risk stocks available, these are the so called "blue chip stocks". However, because of the low risk factor, the chance for substantial gains can be minimal compared to a stock with a higher risk factor.

Similarly, capital depreciation or appreciation can be a factor in the investment performance of a mortgage or bond fund. You may wonder how a mortgage or a bond which is usually for a fixed sum of money can change in value and an illustration may serve to explain this. Let us assume the pension fund has purchased, as an investment, a five year mortgage with a 16% interest rate. Obviously the 16% is a fixed rate for the next five years and the pension fund can therefore be assured of an income component on their investment of at least 16%. However, let us say that after two years mortgages are now going for 18%. The pension fund wishes to dispose of their investment in the 16% mortgage. However, as you can see it would be very difficult to dispose of such a mortgage because why would someone purchase a 16% investment when they can go out on the market place and buy an 18% investment. Therefore it would be necessary to drop the price of the 16% mortgage so that it would in fact give the new investor an overall yield of 18%. Therefore in times of rising interest rates the capital portion of a mortgage or bond investment will decrease and, similarily, in times of falling interest rates the capital portion of these investment will increase.

The last two investment categories, guaranteed investments and commercial paper, are both fully guaranteed as to principal and interest.

As can be seen from the foregoing comments the matter of pension fund investments is very complicated and is best left to professionals. There are very few, if any, pension fund trustees who would have sufficient expertise to be able to decide on questions such as which stocks to buy or sell, when to buy or sell them, how many to buy or sell, which mortgages to purchase, which bonds to purchase etc. These decisions are the ones that need the expertise available from any competent investment manager.

This is not to say that the trustees and ultimately the members have no say or control in where and how their pension funds are invested. The trustees certainly have the right to set certain restrictions on the investment manager. For example, the trustees may direct that no more than 25% of the pension fund, at any given time, be invested in equity type securities. Another restriction that could be set is that the investment manager could be directed to ensure that no holdings of the fund (equities, bonds, etc.) be in a competitive firm in the same industry.

Remember, it is the trustees who have the ultimate responsibility for the investment of the pension fund, and while the rate of return is ideally at a maximum, the safety or the risk factor of the investments could be said to be an overriding criteria.

The Pension Benefits Act of Manitoba also has regulations pertaining to allowable investments of pension funds. These regulations, in general, relate to the security of pension funds by requiring a certain degree of diversity in the holdings. Put another way the Pension Benefits Act ensures that not all the pension fund's "eggs are in one basket".

You Asked Us . . .

Are There Regulations Concerning Interest Rates on Pension Funds?

There are currently no regulations specifying what rate of interest must be paid on contributions to a pension fund. In general, interest paid on contributions is usually quite conservative. This is for three reasons:

1. A pension plan is established for one purpose, and one purpose only, that being to provide the members with a monthly income at retirement. A pension plan is not a savings vehicle and should not be viewed as such. The important thing to remember is that you have been promised a certain amount of pension and that is what you can expect, regardless of the interest paid on contributions.
2. Should the pension fund as a whole earn a rate of interest higher than what is being paid to the members this will allow for extra funds to be accummulated in the pension fund. This surplus can than be used to improve benefits for all the members.
3. As described in the next question, there are laws pertaining to the investment of a pension fund and these laws are aimed at the safety of the investments rather than the rate of return. Because of this, a pension fund may not earn as high as interest as other investments which are much more risky.

Are All Investments Reviewed by the Pension Commission?

All pension plans with employees in Manitoba must be registered with the Pension Commission. This registration insures that each plan is being operated compliance with the Act. Contained in the Act are provisions relating to the investment of pension funds. All investments of the pension fund must be made in accordance with these regulations, thereby guarding against loss through high risk investments. As well, the funding of the pension plan must meet acceptable standards of solvency. The Commission reviews each plan annually to ensure that adequate contributions are being made to provide the promised benefits.

Why are Employees Not Aware of Where Their Contributions are Being Invested?

As mentioned earlier, the decision regarding where the funds of a pension plan are to be invested is one of the duties of the Board of Trustees. Very often the Board of Trustees is made up of representatives solely from the employers. Because of this, members of the pension plan have little or no input into the investment discussions or access to information. This is why it is very important that the employees have a representative(s) on the Board of Trustees to ensure adequate communication to all the plan members.

Can the Employer Invest All the Funds in his Own Corporation?

No. The Pension Benefits Act states that any one holding or investment can not exceed 10% of the total value of the fund.

SECTION 6 - Delinquent Accounts

One of the traditional problems encountered with multi-employer plans is the fact that one or several employers may be in default in remitting payments to the trust fund.

This can occur for a variety of reasons including:

- poor economic condition of the industry
- competition from non-union firms
- bad business practices of employers who do not know their costs, and who ultimately go out of business.
- unwillingness of union and business representatives to take action provided for in the collective bargaining agreement
- lack of provisions in the trust agreement allowing for enforcement
- "laissez-faire" attitude of trustees and administrators — late payments will always exist and should be accepted
- poor follow-up procedures on late payments
- when interest rates are high borrowed money is expensive and delinquent contributions are a cheap source of capital for employers

Effective controls for following-up and collecting delinquent contributions must be established. While some of the reasons mentioned above cannot be controlled by the trustees, proper administrative procedures will ensure that constant checks are being made of remittances and any delinquencies will not go unnoticed for long periods of time.

A second method which could be used would be regular reporting to plan members of their benefits to date. Members should be asked to check these against their own payroll records and any complaints which arise from noticed discrepancies should be investigated promptly.

A third and the most complicated method would be a payroll audit. Most trust agreements empower the trustees with the ability to have such an audit performed. This would generally be done by outside professionals i.e. chartered accountants.

The auditors will examine the books and records of either all or selected employers and will then submit to the trustees a report comparing the actual hours worked with hours reported. Any discrepancies should again be investigated promptly.

The previous paragraphs have dealt with why delinquencies occur and how to detect them. We must now look at what to do about them.

Collection of delinquent accounts can be handled in several ways. Examples of these would include the following:

The simplest and easiest method would be to send a notice of delinquent account to the employer in question requesting the amount required to be

paid and a deadline for payment. If payment is not made, a second method could be followed — that of legal action.

The delinquent employer can be referred to a lawyer who will examine the case to determine the cause for the non-payment and explore possible ways to reconcile the dispute. The lawyer will usually attempt to resolve the matter by other methods before filing suit, however, this action may be necessary in order to reclaim unpaid funds.

Another example of how to ensure employers pay the proper amounts is to have each employer post a cash bond upon entering the plan. This bond could then be used to guarantee any deficient payments.

SECTION 7 · Pension Plan Discontinuance

What Happens If . . .

1. Future negotiations cancel the pension plan.
2. The company is sold.
3. The company (employer) goes bankrupt.

As a preamble to the answers to the above questions this is one of the features of the Pension Benefits Act of Manitoba and Regulations to protect the employee pension benefits earned under the terms of the pension plan. This is done by requiring all pension plans to be registered with the Commission. Before registration can be approved, the pension plan must contain all the provisions which are stipulated in the legislation. In addition, we must have copies of all other pertinent documentation such as: the trust agreement, the most recent negotiated agreement, the employee pension plan booklet, the actuarial valuation which certifies the method of funding thereof and a cost certificate which specifies the contributions which will be made by the members, where applicable, and the contributions that are to be paid by the employer(s) to pay for the pension benefits each year. If the plan has a liability, which would occur if the benefits for prior years were to be increased, the required payments are to be shown and they are to be paid within the period prescribed by the regulations.

To monitor the ongoing status of the pension plan the trustees or plan administrator must file an Annual Pension Plan Information Return with the Commission. This return along with other information certifies as to the actual contribution paid to the plan fund for the year under review. This is compared to the contributions that were to be made in accordance with the cost certificate filed with us earlier.

The regulations require any member contributions to be remitted to the plan fund no later than 60 days after they have been deducted from the employee earnings. If the negotiated agreements call for a shorter time period that is what must occur. With this background information you will see that there are controls to protect the benefits you are accruing under the pension plan of which you are a member.

1. **Future negotiations cancel the pension plan.** If sometime in the future the union and the employer(s) agree not to continue the negotiated pension plan then the plan is effectively terminated. When this happens the Commission declares this a plan wind-up and all assets of that plan are to be fully vested in the benefits earned to the date the negotiated agreement terminating the plan takes effect. All required contributions to the termination date must be made. If there is no successor plan, the settlement of benefits, in accordance with the pension legislation and the plan, will be made. If there is a successor plan, there is no settlement until an employee's ultimate termination, death, or retirement. There is a possibility that the replacement pension plan undertakes the liabilities of the previous pension

plan. In this case all assets backing the benefit earned under the former pension plan could be transferred to the new plan.

2. **The Company is sold.** If the company is sold prior to the expiration of the negotiated agreement the pension plan must continue in force as contractually provided for. The pension plan also continues beyond the expiry date of the agreement if the union has so indicated in writing to the employer, before the expiration date, that they wish to negotiate.

   Whether or not the plan continues in force with the new employer will be in accordance with the negotiations. If the pension plan will not be continued, the pension benefits will be fully secured and settlements can only be made in accordance with the Act and the pension plan provisions.

3. **The Company (employer) goes bankrupt.** Once we are advised that a firm has gone into bankruptcy we immediately contact the trustees or fund administrator to check whether or not all required contributions up to the declared bankruptcy date have been made. If they have been made the benefits to date are secured. If there is a shortage of required contributions we contact the trustee in bankruptcy and advise them that they are on notice to pay any and all contributions that were required to be made in accordance with the agreement up to the date of bankruptcy. In the event the plan is officially terminated on the declared bankruptcy date, all benefits are to accrue fully to the plan member again in accordance with the most recent agreements and the Pension Benefits Act.

In conclusion, it can be seen that there are provisions to protect the pension benefits earned by the member's by policing of the plan while it is active as well when circumstances disrupt the program in any way from what was the intent at inception. The main intent is, as you know, to accrue a pension while you are working so that you can retire in dignity. The Pension Benefits Act provides the legislation to protect those benefits both while the plan is in force and if it is terminated in any manner.